The rights of investors in unit trusts

Unit trusts have become an increasingly attractive option for savers, now that bank deposits earn negative returns in real terms, with inflation rates rising above interest rates offered by commercial banks. To be sure, higher returns on investments are not the only reason why one might want to resort to unit trusts.

Of late, unit trust funds have become a more popular choice for personal wealth accumulation. This trend is not surprising when one considers the advantages of investing in unit trust funds. Take for example diversification, which allows the unit-holder to invest into a pool of funds rather than limiting his/her portfolio to a single investment. Also, the unit-holder can gain exposure to particular asset class or investments not accessible to a small investor. Besides, the unit-holders may find some comfort in the fact that the unit trust funds are managed by professionals with knowledge, skill and experience.

After all, the minimum initial investment amount for most unit trust funds is relatively small, thus making them affordable compared to direct investment in securities. Yet another advantage of unit trust funds is liquidity, as the units held in a unit trust fund may be sold to the fund manager on any business day, hence, making it easy for the unit-holder to realise his/her money should the need arise. This compares favourably with investments in fixed assets such as land and properties that take a relatively longer time to liquidate.

However, before a potential investor decides to take the plunge, he or she must also be aware of the risks and costs that unit-trust investments entail. As with any other type of investment, investing in unit trust funds also carries its own risks, including interest rate risk and management risk. To this one must add loss of control, as one does not have the right to direct how one’s savings in the unit trust fund are invested, as long as the fund manager is managing the unit trust fund in accordance with the prospectus and deed. What is more, there is a price tag for the services provided by the fund manager, which means that the fees and charges payable to the unit trust management company do affect the unit-holder’s returns.

On a positive note, a unit trust holder is accorded many rights similar to those of a shareholder, such as the right to receive a distribution of income and the right to attend and vote at meetings. These rights are mostly defined by the deed which performs a similar function to the memorandum and articles of a company. But the point of difference concerns the nature of the interest of the shareholder on the one hand and the unit-holder on the other.

The trust deed defines the nature of interest the unit-holder has in the assets of the trust as a beneficiary and not that of the owner of a separate piece of legal property as is the case with shareholders. It is equity which defines the nature of that interest which is enforceable against the trustee.

Under the eyes of the Securities Commission and Inland Revenue Board, a fund is a legal entity. A fund is, therefore, liable to taxation and can be moved from one unit trust management company to another for management purposes, if need be.

Although the distinctions outlined above are not always easy to draw, the inherent rights of the unit-holders are duly recognised and upheld. The rights of unit-holders are generally provided in the deed or the prospectus of the unit trust fund. In addition, unit-holders may have rights that are provided under the law or in equity. For starters, unit-holders are entitled to receive distributions of income and capital through the trust fund, according to the number of units they hold, and to participate in any increase in the value of the units, as provided by the deed. The deed also provides that unit-holders have the right to appoint, as well as remove, the trustee or fund manager of a unit trust fund by calling for a meeting of unit-holders and vote for the removal of the trustee or fund manager through an extraordinary resolution. In addition, unit-holders have a common general right to demand full, clear reporting from the management.

As the unit trust funds are managed by professional fund managers, the unit-holders have a right to be provided with responsible investment recommendations by their unit trust advisers based on their personal objectives, time horizon, risk tolerance and such other relevant factors which they have disclosed. Unit-trust advisers are obliged to provide professional assistance in helping unit-holders clarify their investment goals and risk tolerance levels. Unit-holders can count on their unit-trust advisers' assistance in setting realistic expectations about the long-term performance and associated risks of various securities. It is the duty of unit-trust advisers to present the unit-holders with reasonable investment alternatives designed to meet those expectations and disclose the comparative risks, benefits and costs.

As market sentiment is the thrust for the returns on investment in unit trusts, unit-holders have a right to have regular meetings with unit-trust advisers in order to determine whether there is a need for asset re-allocation or increase in the existing investment portfolios. There are "cooling-off rights" as well. First time unit-holders are entitled to a cooling-off period of six business days from the date of purchase of the units. Should there be a change of mind about the investment, one may exercise one's cooling-off rights, whereby monies paid by the unit-holder for the investment will be returned within ten days of receipt of the cooling-off notice.

Reference may also be made to the so-called "switching facility" which represents a convenient way for the unit-holders to convert units of one fund into units of another fund managed by the same fund manager in response to changing financial goals and market conditions. This facility is usually subject to payment of an administration fee as prescribed by the fund manager, although some funds do allow one or two free switches a year. This, in any case, is much cheaper than redeeming one's units and immediately purchasing another fund with the same or a different fund manager. It is also worth noting that one may transfer the units registered in one’s name to other persons, should the need arise, subject to payment of an administration fee as prescribed by the fund manager.

All this does not necessarily mean that things cannot go wrong in the unit trust business. But then there are some safety valves in the form of channels to the fund managers or the Federation of Malaysian Unit Trust Managers, which allow unit-holders to lodge their complaints of any misconduct or wrongful selling against unit-trust advisers.